

Comments of the Division of the Ratepayer Advocate Concerning Rate Equalization and Lost Revenues

I. Rate Equalization

The New Jersey Clean Energy Program is an outgrowth of the Electric Discount and Energy Competition Act of 1999 (EDECA), which created the current structure of the State's electric and gas supply and distribution system. Section 12.a of EDECA created legislatively mandated public benefits charges to support State energy policies. It mandated funding for energy efficiency and renewable energy programs in order to yield public benefits, in particular economic and environmental benefits. The new programs were initially known as Comprehensive Resource Analysis or "CRA" programs, and are now known as the New Jersey Clean Energy Program or "CEP".

Funding for the CEP is collected by the distribution utilities through surcharges to their customers, yet it must be treated in a separate and distinct fashion from rates based on the costs of utility services. The Clean Energy Program is operated on a statewide basis under the overall authority and oversight of the Board of Public Utilities (Board or BPU) and its Office of Clean Energy (OCE). Since the Clean Energy Program is operated in a statewide mode, there should be no variation in the surcharge for energy efficiency programs by utility service area. Surcharges to support efficiency funding should be the same, per-kWh or per-therm, for all the State's distribution utility customers. This is equitable, since the environmental and economic benefits of energy measures benefit all New Jersey consumers statewide.

Utility-specific discrepancies in levels of funding for demand-side energy programs are historic in nature, dating from the period before EDECA. In its initial Order implementing the Clean Energy Program, the Board continued the historic pattern of differing funding levels by utility.¹ Thus, at the current time, CEP surcharges still vary by utility service area. However, it is important to note that EDECA itself, in setting terms for funding for energy efficiency and renewable energy programs, expressed all funding minimums in Section 12 in terms of "Statewide funding." Moreover, the Board has called for comments on equalizing the level of support for the CEP among the various utilities for the year 2004.² This proceeding creates an opportunity to correct the historic anomaly of unequal levels of support for CEP across the State.

¹ *I/M/O the Petition of the Filings of the Comprehensive Resource Analysis of Energy Programs Pursuant to Section 12 of the Electric Discount and Energy Competition Act of 1999*, BPU Docket No. EX99050347 (Generic) *et al.*, (Final Decision and Order, March 9, 2001) ("March 9, 2001 Order").

² *I/M/O Appropriate Utility Funding Allocation for the 2004 Clean Energy Program and I/M/O Comprehensive Energy Efficiency and Renewable Energy Resource Analysis*, BPU Docket Nos. EX03110946 and BPU Docket No. EX04040276 (Order Establishing Procedural Schedule Issues to Be Addressed, May 7, 2004).

Equalizing CEP funding involves two steps. First, the funding responsibility needs to be reallocated among electric and gas ratepayers. Then, based on that allocation, the surcharges for electric and gas ratepayers need to be equalized.

For 2004, we believe a transitional approach is needed. Some movement toward rate equalization should occur, but full equalization could wait until the year 2005. Specifically, we suggest leaving the electric/gas split as it is for the year, while beginning the rate equalization process among the different utility service areas. Since the year is almost half over, we suggest equalizing the electricity CEP surcharge and the gas CEP funding rates for the second half of 2004. Also, July 1, 2004, is the effective date of OCE administration of the entire CEP, and is a logical time to move away from CEP funding rates that vary by service area.

1. Electric/Gas Funding Allocation

In December 2003, the Board established the interim 2004 CEP budget of \$124.126 million.³ It also established the utilities' payment obligations for the CEP for 2004, providing a month-by-month payment schedule for each electric utility and each natural gas utility.⁴ The electric utilities' obligations total to \$90.294 million of the interim 2004 CEP budget of \$124.126 million, or 72.7%. The natural gas utilities' obligations total \$33.833 million, or 27.3% of the interim budget.

Since the first half of the year is almost complete, it is useful to look at the utility payment obligations established by the Board for the second half of 2004. For that period, the electric utilities' obligations total to \$48.807 million of the July-December 2004 CEP budget of \$63.864 million, or 76.4%. The natural gas utilities' obligations total \$15.057 million, or 23.6% of that budget.⁵

For 2005 and subsequent years, the Board should consider whether this electric/gas split should be retained, or whether there is some basis for a different split. One basis for allocating CEP revenue responsibility between electric and gas ratepayers might be the total amount of revenues, including commodity, collected from electric and gas ratepayers. The Ratepayer Advocate offered this approach in 1999 testimony in the CRA proceeding.⁶ PSE&G also

³ *I/M/O the New Jersey Clean Energy Program -- 2004 Programs and Budget*, BPU Docket No. EO02120955 (Order, December 22, 2003).

⁴ *I/M/O the New Jersey Clean Energy Program -- Fiscal Agent*, BPU Docket No. EO02120955 (Order, December 23, 2003).

⁵ Calculated from Order cited in note 4.

⁶ *I/M/O the Filings of the Comprehensive Resource Analysis of Energy Programs Pursuant to Section 12 of the Electric Discount and Energy Competition Act of 1999*, BPU Docket No. EX99050437 et al. (Direct Testimony of Dr. David Nichols, filed August 23, 1999). It should also be noted that Dr. Nichols' testimony was based on data from the period before rate unbundling when the total commodity costs were not as transparent as in today's unbundled services.

suggested this in its comments in this proceeding.⁷ However, there may be difficulties in applying this approach, now that some of the data regarding electric or gas energy from third-party suppliers may no longer be available and could not be included in the calculation. Including commodity costs also implicates the problems inherent in the current volatility in natural gas prices and the year-to-year variation in the costs for natural gas that are passed through to gas utility customers taking the Basic Gas Supply Service.

A possibly preferable basis for allocating CEP revenue responsibility between electric and gas ratepayers might be the amount of utility revenues, excluding commodity. JCP&L suggests this approach in its comments in this proceeding (but only for application from 2005 on).⁸ This approach has the benefit of being based on the ready availability of complete data.

The first two approaches are “top down,” allocating a given pool of dollars based on an electric/gas allocation factor. Another approach could be “bottom up.” In this approach, a reasonable suite of programs would first be developed with their associated market penetration targets and funding levels. Then, the costs for the electric energy efficiency and renewable energy programs would be collected from electric utility ratepayers, and the costs for the gas energy efficiency programs would be collected from gas utility ratepayers.

The second and third of the three alternatives just described should be considered for 2005. These options will be further addressed in the Ratepayer Advocate comments concerning CEP funding for 2005-2008.

2.A. CEP Rates and Utility Totals--Electric

We can estimate the uniform statewide CEP rate required to collect \$48.807 million from electric ratepayers. For this purpose, we can use the forecasts of electric sales for the year beginning July 1, 2004, as filed in the current BPU dockets to establish permanent Universal Service Fund rates.⁹ Total electric sales of 39,325,923,000 kWh are forecast for the period from July 1, 2004 through December 31, 2004. This implies a uniform statewide electric CEP surcharge of 1.24 mills/kWh. Using the same sales forecasts, each electric utility would now be responsible to collect the amounts shown in the below table for the CEP for the second half of 2004. The table compares the current schedule of monthly payments with a new one based on the equalized CEP charge.

⁷ *I/M/O Appropriate Utility Funding Allocation for the 2004 Clean Energy Program, BPU Docket No. EX0310946* (PSE&G Initial Statement, January 21, 2004, page 2).

⁸ *I/M/O Appropriate Utility Funding Allocation for the 2004 Clean Energy Program, BPU Docket No. EX0310946* (JCP&L Initial Statement, January 21, 2004, pp. 1-2).

⁹ *I/M/O the 2004/2005 Annual Compliance Filing for an Increase in the Statewide Electric and Gas Societal Benefits Charges (SBC) Rates Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1 – Public Service Electric and Gas Company, BPU Docket No. EX00020091, Attachment A, Page 7 of 9.*

2.B. CEP Rates and Utility Totals--Gas

We can estimate the uniform statewide CEP rate required to collect \$15.057 million from gas utility ratepayers. For this purpose, we can also use the forecasts of utility gas sales for the year beginning July as filed in the current BPU docket on USF rates. Total gas sales of 1,941,375,000 therms are forecast for the period from July 1, 2004 through December 31, 2004. This implies a uniform statewide gas CEP surcharge of 7.76 mills/therm. Using the sales forecasts from the same USF docket, each gas utility would be responsible to collect the amounts shown in the below table for the CEP for the second half of 2004.

2.C. Table Comparing Utility Payments With Equalized Rates to Current Payment Schedule

	CEP Payments (Thousand \$)		
	Current	New	New/Current
Conectiv	6277	6282	1.00
JCP&L	19014	13971	0.73
PSE&G - E	23228	27507	1.18
RECO	288	1046	3.63
All electrics	48807	48807	1.00
NJNG	1850	2275	1.23
NUI	1900	2217	1.17
PSE&G - G	9645	8796	0.91
SJG	1662	1769	1.06
All gas	15057	15057	1.00
TOTAL	63864	63864	

2.D. CEP Final Budget for 2004

The above proposals and calculations are based on the interim CEP 2004 budget of \$124.126 million. In Comments to the Board, the Ratepayer Advocate recommended increasing the final 2004 CEP budget by \$15 million.¹⁰ If the Board accepts this recommendation, it should be implemented consistently with the adoption of equalized electric and gas funding rates for the second half of 2004, as described above.

¹⁰ *I/M/O Appropriate Utility Funding Level for the 2004 Clean Energy Program, BPU Docket No. EX0310945* (Ratepayer Advocate Comments, April 30, 2004).

II. Lost Revenues

1. Background

Under the DSM regulations adopted by the Board before the passage of EDECA, utilities could recover revenues “lost” due to their operating certain types of energy efficiency programs. Revenues can be “lost” when sales are reduced from energy efficiency programs, and the utility’s savings in variable costs do not fully compensate for such lessened sales revenues. Since the passage of EDECA, the Ratepayer Advocate has consistently held the view that provision for utility “lost” revenues should not be available as a result of section 12 of EDECA. Our view was, and remains, that EDECA moved us from the framework of past DSM regulations, which were founded on the need to *induce* utilities to aggressively procure demand-side resources, to the framework of section 12, which *mandates* that funds collected from ratepayers be used to support new energy efficiency and renewable energy programs. Indeed, since utilities desired to administer the EDECA-mandated programs, we were surprised when, in 2000, several requested reimbursement for net “lost” revenues for the new programs. Our view was that there are benefits to utilities (but not necessarily ratepayers) from the utilities administering energy efficiency programs, as such programs are generally well-received by their customers, and contribute to deferring the need for utility investments in distribution plant.

With the enactment of EDECA, the Board was directed to undertake a comprehensive review of the utilities’ existing energy efficiency programs, to determine the appropriate level of ratepayer funding for energy efficiency measures, and to establish the appropriate funding levels for new programs to promote the development of renewable energy sources. In its *March 9, 2001 Order*, the Board decided the specific CRA (now CEP) programs and budgets to be implemented by the utilities through the end of 2003. In that order, the Board adopted the Utilities/NRDC Stipulation, which allowed lost revenue recovery for new energy efficiency programs, but not for renewable energy programs. This recovery would not count as a new program cost, and would only be in effect through 2003. *March 9, 2001 Order* at 73. The Ratepayer Advocate was not a party to this stipulation. This office had proposed the Board adopt a stipulation that allowed no lost revenue recovery for new programs at all. However, the Board chose to adopt the Utilities/NRDC Stipulation, meanwhile noting that:

Lost revenue recovery and incentives were allowed under the DSM regulations only for programs with measured and verified savings. The amount of fixed cost revenue erosion resulting from energy efficiency measures can be significant and it is therefore important for the calculation of these costs to be accurate. This need for accuracy is the reason the Board was historically unwilling to allow the recovery of lost revenues for programs that did not have verified, measured savings. *Id.*

The Board also directed that recovery for lost revenues that were a result of new programs would be subject to the Board’s approval of the calculation methodology prior to their eligibility for collection. *Id.* at 77. The utilities submitted proposed protocols for measuring energy savings impacts from the Clean Energy Program to the BPU on July 1, 2001. Revised

protocols were distributed for a meeting at the Board on May 20, 2003. Based on discussions at that meeting, utilities staff undertook to consider over 40 action items and propose further revisions to the protocols as appropriate. This led to the *New Jersey Clean Energy Protocols, June 2003* (the “*Protocols*”).

In light of the above considerations, we believe that the scope of consideration for compensating utilities for “lost” revenues must be confined to the limited categories arising from the Board’s *March 9, 2001 Order*. There must be no “lost” revenue compensation for any Clean Energy Program from 2004 onward.¹¹ “Lost” revenue compensation must be limited to 2001-2003 energy efficiency programs shown to have caused substantial and measurable reductions in energy consumption. Programs of an education/training/information nature should not be eligible; such programs help “sell” programs that do have measurable impacts, but did not receive “lost” revenue recovery under the DSM regulations of the past. Also excluded should be the low-income energy program, which may be considered an on-going social obligation, and for which lost revenues have never been awarded. Finally, on-site renewable energy programs should be excluded, as the precedent of awarding electric utilities revenues lost to distributed generation could result in time in substantial increases to rates outside the context of base rate hearings. The fundamental remedy for a utility whose income has sagged due to sales level or cost levels is to apply for a base rate hearing in which all aspects of revenues and the cost of service can be reviewed in a comprehensive manner.

2. Determining Lost Revenues Through Impact Evaluations

The OCE has adopted the *Protocols* for purposes of tracking the CEP’s estimated impacts on energy use. We believe the *Protocols* are reasonable tools for that purpose. However, the *Protocols* have not been adopted by the OCE or the BPU for purposes of establishing “lost” revenues from CEP programs during 2001 - 2003. In our view, the *Protocols* are not appropriate tools to establish utility lost revenues for several reasons.

The *Protocols* are engineering estimates used to prospectively estimate the energy savings that will accrue from measures installed through the CEP. There is some post-installation verification that custom projects or large complex jobs have been installed as planned. But other than that --and unlike the measurement protocols formerly used in the “Standard Offer” programs of the past-- there is no on-going measurement to establish the effects of installed program measures on energy use over time. Such on-going measurement in itself is not sufficient to establish the actual effects of program measures on energy sales. But it is a necessary aspect of evaluating the impact of programs with a high degree of accuracy, and it is not yet part of the CEP.

Measurement of the effects of installed CEP measures on energy use over time can help to establish how the actual operational savings from efficiency measures compares with the initial engineering estimates of anticipated savings (which are all that are in the *Protocols* now). But it is also necessary to evaluate how much of the efficient equipment installed through the

¹¹ These Comments do not address the issue of lost revenue recovery from legacy DSM programs, which we understand to be outside the scope of the instant proceeding.

CEP would have been installed anyway if the programs did not exist. There is some underlying trend of efficiency improvement in the market due to technology, price, and policy forces. The *Protocols* do not take full account of this trend. Indeed, sophisticated surveys of participants in the CEP, non-participants, and/or trends in regional and national markets are needed to establish plausible “baselines” of underlying efficiency improvement, which must be deducted from CEP-induced efficiency improvement to establish the net CEP effect on energy sales. There are well-established methods for performing such studies. But so far they have been applied to only one part of the CEP, the low-income program.

The fundamental process used to establish the best possible assessment of net energy savings is called *impact evaluation*. Impact evaluation includes both measurement of energy use after the installation of efficiency program measures, and a variety of tools to establish how much energy efficiency improvement would have occurred in the market without the existence of energy efficiency programs. With one exception, impact evaluations of the CEP have yet to be carried out. Without them, we do not have sufficiently accurate estimates of the revenues utilities may actually have lost as a result of the CEP.

The Ratepayer Advocate’s consultant, Dr. David Nichols, participated in meetings on the *Protocols* that were hosted by the Board. He also testified in JCP&L’s last base rate case (BPU Docket No. ER02080506). In both of these venues he expressed and documented concerns about several elements of the *Protocols* that tend to overestimate the energy savings achieved by program measures. Some of these concerns were addressed in the *Protocols* revisions of June 2003, while others were not. In particular, the very fundamental issue of what efficiency improvements may have occurred in the market without the CEP in place, as determined by professional impact evaluation, is simply beyond the scope of the *Protocols*.

As the Board recognized in its *March 9, 2001 Order*, before charging the ratepayers for revenues “lost” through the CEP, it is necessary to have a high degree of accuracy in quantifying lost revenue. The standard for lost revenue recovery must be higher, and more “conservative”, than the standard for estimating efficiency program impacts for general reporting purposes. Because of their inherent limitations, the *Protocols* do not provide the required level of accuracy. Only professionally conducted impact evaluations would suffice.

The Board should defer awarding lost revenues until professional impact evaluations have been conducted. Such evaluations should provide specific results concerning utility lost revenues during 2001 - 2003 for the programs for which utilities seek lost revenue recovery.

3. Utilities’ Estimates of Lost Revenues

The utilities should submit their estimates of CEP lost revenues at the June 8 hearing in this matter. It is difficult for the Board to make informed decisions without a comprehensive estimate of the amount of dollars and the rate impacts claimed by the utilities as a consequence of applying the *Protocols* to the calculation of lost revenues. Ratepayers also deserve notice of the dollar impacts on them that would come from the utilities’ proposal for lost revenue recovery. The utilities should also submit the underlying calculations used to estimate CEP lost revenues.